93-207. CASE NO. _____

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SUPREME COURT OF THE UNITED STATES

OCTOBER 1993 TERM

JESS KRAFT AND BARBARA KRAFT,

PETITIONERS,

v.

UNITED STATES OF AMERICA,

RESPONDENT.

_____/

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

PETITION FOR WRIT OF CERTIORARI

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QUESTIONS PRESENTED

Whether Appellants/Petitioners have set forth a genuine issue of material fact relevant to their suit pursuant to 26 U.S.C. §1341 wherein they sought the application of the claim of right doctrine to a restitution payment made to Blue Cross/Blue Shield of Michigan.

Whether the Sixth Circuit Court of Appeals erred in affirming the granting of summary judgment in favor of the United States by the District Court for the Eastern District of Michigan as to Appellants/Petitioners' claim for relief pursuant to 26 U.S.C. §1341.

Whether a split in the manner the United States Circuit Courts are treating certain restitution payments for tax purposes exists which must be rectified so that consistent treatment can be provided to all taxpayers.

Whether the lower courts properly addressed the application of IRC §1341 to restitution payments made in the face of unproved allegations of fraud as distinct from embezzlement.

Whether the decision of the Court of Appeals for the Sixth Circuit departs from the accepted and usual course of judicial proceedings, or sanctions such a departure by the District Court for the Eastern District of Michigan, so as to call for exercise of this Court's power of supervision.

Whether the United States Court of Appeals for the Sixth Circuit has decided an important question of federal law which has not been, but should be, settled by this Court.

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OPINIONS OF LOWER COURTS

A. On March 2, 1992, Senior Judge Robert E. DeMascio of the United States District Court for the Eastern District of Michigan issued his written Order and Judgment whereby summary judgment was granted to the United States. A copy is included in the Appendix.

B. On April 7, 1993, the United States Court of Appeals for the Sixth Circuit, through Senior Circuit Judge Conti, affirmed the decision of the District Court. Chief Judge Merritt and Circuit Judge Nelson issued separate, concurring opinions. The Opinion (and concurring Opinions) are included in the Appendix.

STATEMENT OF JURISDICTION

Appellants/Petitioners seek review of the Opinion of the United States Court of Appeals for the Sixth Circuit, Case No. 92-1552, decided and filed on April 7, 1993. The statutory provision granting this Court jurisdiction to review the Judgment in question by Writ of Certiorari is 28 U.S.C. §1254.

RELEVANT STATUTE

26 U.S.C. §1341:

a) General Rule - If:

(1) an item was included in gross income for a prior taxable year (or years) because it appeared that the taxpayer had an unrestricted right to such an item;

(2) a deduction is allowed for the taxable year because it was established after the close of such prior taxable year (or years) that the taxpayer did not have an unrestricted to such item or to a portion of such item; and

(3) that the amount of such deduction exceeds $3,000,

then the tax imposed by this chapter for the taxable year shall be the lesser of the following:

(4) the tax for the taxable year computed with such deduction; or

(5) an amount equal to -

(A) the tax for the taxable year computed without such deduction, minus

(B) the decrease in tax under this chapter (or the corresponding provisions of prior revenues laws) or the prior taxable year (or years) which would result solely from the exclusion of such item (or portion thereof) from gross income for such prior taxable year (or years).

SUMMARY OF THE ARGUMENT

In our respectful opinion, the lower courts have erred their findings for the following reasons:

1. Inasmuch as the indictment accused the xpayer of fraudulently obtaining $84,160 and the taxpayer, as part the plea arrangement, reluctantly agreed to acknowledge the audulent receipt of $19 (included in a check from Blue Cross in the nount of $1,358), there is clearly a factual determination to be ade as to what amounts, if any, were obtained by fraud. The wer courts' assumption (voiced, but not written) that if the payer agreed to repay the $160,000 to Blue Cross then it must ve all been fraudulently obtained is baseless and incorrect. Absent Government being able to prove fraud in excess of that $19 ount, it should not be allowed to prevail in refusing to provide the payer claim of right treatment for all amounts not proved to have n fraudulently obtained. Permitting the summary judgment to

stand in this instance would further the departure from the accepted and usual course of judicial proceedings to have factual disputes decided by the trier of fact. This Court should exercise its power of review to rectify this error.

2. The taxpayer was "persuaded" to enter into to plea arrangement. The club used by the Government was the reat that if he did not agree to accept the plea arrangement that it ould be requesting a sentence of life imprisonment without parole. that the taxpayer never had any previous criminal record hatsoever, almost any alternative was acceptable. Understanding is, it is most unreasonable to assume that because the taxpayer reed to the repayment to Blue Cross of $160,000 as a condition of t plea agreement that there was any tacit admission in such reement that he had committed such fraud. This case never went trial; therefore, neither the Federal District Court nor the Court Appeals has any definitive information as to the extent of the ual fraud, if any. As such, at a very minimum, this case cannot decided by summary judgment and must be remanded to the

strict court for a determination of the extent of the fraud. rmitting the summary judgment to stand in this instance would rther the departure from the accepted and usual course of judicial oceedings to have factual disputes decided by the trier of fact. is Court should exercise its power of review to rectify this error.

3. The lower courts' erroneously relied primarily the dictum contained in *Bailey v. Commissioner* 756 F.2d 44 (6th . 1985) (i.e., "repayment did not arise from the specific circum- nces, terms and conditions of the transaction whereby the amount s originally included in income"). Had Dr. Kraft paid the money his corporation and the Corporation in turn paid the money to e Cross, the Government's argument based on *Bailey* would not st. Unlike Mr. Bailey, the salary paid to Dr. Kraft was substan- y his portion of the amounts received from Blue Cross. There- , for the Government to take the "form over substance" approach expect that the taxpayer under threat of a life sentence without ole would be overly concerned with the tax ramifications of the agreement is manifestly unjust. However, inasmuch as the

payment does comply with the provisions of IRC §1341, the Government should not be allowed to apply the *Bailey* dictum. The resolution of this issue encompasses an important question of federal law which has not been, but should be, settled by this Court.

4. As it relates to this matter, the taxpayer had the misfortune to live in the Sixth Circuit, which having decided *Bailey* appears now to be "hidebound" to follow it. That decision is in conflict with both *Stephens v. Commissioner*, 905 F.2d 667 (2d Cir. 1990) and *Joseph A. Barrett*, 96 T.C. No. 31 (1991). The taxpayer is not arguing that the decision in *Bailey* was incorrect, but rather that the portion of that opinion relating to that court's interpretation of IRC §1341 wherein it held that the "repayment did not arise from the specific circumstances, terms and conditions of the transaction whereby the amount was originally included in income" was dictum and that its application in the instant case is erroneous. Further, the courts' characterization of the restitution payment as payment of a penalty under *Bailey* is improper and further conflicts with *Stephens*. In that a split exists in the manner

the United States Circuit Courts are treating restitution payments for tax purposes, this Court should exercise its discretion and address the issue so that consistent treatment will be received by all taxpayers.

5. In essence, the decisions of the lower courts in this action have had the effect of using the tax laws to punish the Appellants a second time (by denying them the deduction which they would otherwise be entitled to pursuant to IRC §1341), something this Court has expressly prohibited in *Commissioner v. Tellier*, 383 U.S. 687 (1966).

I.

STATEMENT OF THE CASE

This matter is before the Court on petition for writ of ertiorari to review the granting of summary judgment in favor of e Defendant/Appellee and affirmation by the United States Court Appeals for the Sixth Circuit. Appellants filed this action in the nited States District Court for the Eastern District of Michigan on about November 27, 1990, seeking a refund of taxes paid on come received, which income the taxpayers subsequently found ey did not have an unrestricted right to and had to return. Juris-ction was founded under 28 U.S.C. §1331 and 28 U.S.C. 346(a)(1). In addition, taxpayers sought a deduction for legal fees curred in defending a federal indictment brought in connection th Appellant's medical practice. The parties filed cross-motions summary judgment. The district court granted Appellants' mmary judgment as to the attorney fee deduction. That ruling was appealed. However, the district court granted Appellee summary gment as to the tax refund claim (wherein Appellants seek

application of 26 U.S.C. §1341 to the amounts returned). The Sixth Circuit Court of Appeals affirmed. Appellants seek relief from those orders in this forum.

The background facts of this action are not complicated. From about December, 1973 through September, 1985, Appellant, Jess Kraft (hereinafter "Kraft"), practiced podiatry at Joel H. Haber D.P.M. and Jess Kraft, D.P.M., P.C., a Michigan professional corporation (hereinafter the "Corporation"). Kraft, at all relevant times, was a 50% shareholder, officer and director of the Corporation. During that same time period, Kraft performed medical services including surgical and non-surgical procedures on patients who were covered by medical insurance through Blue Cross/Blue Shield of Michigan, a non-profit Michigan corporation (hereinafter "Blue Cross"). Payment for services rendered to Blue Cross was generally made by Blue Cross directly to doctors Haber and Kraft, individually, and they then deposited those monies into the Corporation.

Specifically, from about January 1, 1981 through April 1, 1985, Kraft, along with Dr. Joel Haber, billed Blue Cross

for medical services, including non-surgical and surgical procedures performed on patients by Kraft and Haber, in the approximate amount of $2,262,350. During that same time period, for the fiscal years ending August 31, 1981, August 31, 1982 and August 31, 1983, Kraft received a salary of approximately $235,000, $210,000 and $249,000, respectively. Appellants reported this salary for each of the above fiscal years and paid the appropriate federal income tax due on the income (after reporting and taking those deductions and credits allowed by law) and timely filed federal income tax returns.

This matter arose as a result of a federal indictment issued against Kraft and the Corporation on September 14, 1984, charging, among other items, distribution of a controlled substance and engaging in mail fraud. On or about August 13, 1983, Kraft had performed a non-surgical procedure (an x-ray) on a patient who had produced a current Blue Cross card [but whom Kraft later discovered (after rendering the service, but before he forwarded the bill to Blue Cross) not to be the individual named on the card, or an individual covered by Blue Cross]. Nevertheless, Kraft forwarded the claim to Blue Cross. Kraft erred and committed fraud by billing

to Blue Cross for the x-ray cost in the name on the card. For this x-ray, Kraft received $19, which amount was included in a check totalling $1,358 and which was received from Blue Cross. As a result, on April 3, 1985, Kraft and the Corporation, as co-defendants, entered into a plea agreement with the United States of America wherein Kraft pled guilty to one offense of distribution of a "controlled substance" and, upon urgings of his then counsel and the prosecuting attorney, to one count of mail fraud. The mail fraud count involved causing the placement into an authorized depository for mail, to be sent and delivered by the United States Postal Service, the Blue Cross check in the amount of $1,358, which, as indicated above, included $19 for services which were improperly billed.

Additionally, prior to entry into the plea agreement, Kraft, though continuing to maintain that he did not owe Blue Cross, reluctantly agreed to pay Blue Cross $160,000 in settlement, restitution and full restoration of any and all civil claims Blue Cross may have had against Kraft. The restoration payment was for the period of January 1, 1981 through November 30, 1983. Dr. Kraft

was told that if he did not make this payment (and accept all aspects of the plea arrangement), the Government would be requesting a sentence of life imprisonment without parole. As Dr. Kraft recognized that it would be very difficult to successfully do battle on wo fronts simultaneously, the agreement was motivated solely by he desire to avoid litigation with Blue Cross as well as to place Kraft in a more favorable light at the time of sentencing. This estitution amount was paid to Blue Cross. Neither the taxpayer nor ne Government considered the tax ramifications at that time. In ddition to the restitution payment and as part of his criminal entence, Kraft paid to the United States of America $26,000 in iminal penalties.

The money paid to Blue Cross as restitution was erived from the payments received by Kraft from Blue Cross ubsequently placed into the Corporation and then paid to Kraft in e form of a salary). At the time Kraft received those monies from ue Cross he believed, and continues to assert, that he had restricted right to the income and thereby properly reported it as rned income on his tax returns. Kraft timely paid taxes on those

amounts. Subsequently, having made the restitution payment, it became apparent that Kraft no longer had an unrestricted right to the income and sought tax relief pursuant to IRC §1341 for taxes paid on the income which he was forced to disgorge.

It is important to note that the indictment against Kraft alleged that Kraft defrauded Blue Cross of only $84,160. It is additionally important to note that Kraft did not plead guilty to any of these counts and maintains that all services for which these amounts were billed, and all other billed amounts (other than the one instance noted above) were actually performed and the amounts earned. Further, Kraft had not been charged with fraud in excess of this $84,160 amount. Kraft only pled guilty to fraud in submitting a billing in the amount of $1,358 of which he maintains that only $19 was fraudulently received. The lower courts did not make any factual determination with regard to what portion of the $84,160, if any, was obtained by fraud. Appellant asserts that, at the very least, the lower courts erred in not allowing that issue to go to trial. It is Kraft's position that, at the very minimum, he is entitled to IRC §1341 treatment (as will be discussed later) on any amounts repaid

to Blue Cross above this $84,160 amount and, in addition, for any portion of the $84,160 which the Government cannot demonstrate was obtained by fraud. Further, Kraft asserts that any amounts not entitled to IRC §1341 treatment should be treated as a loss incurred in the conduct of a trade or business pursuant to IRC §165(c)(1).

Kraft brought this action in the United States District Court for the Eastern District of Michigan claiming entitlement to federal income tax relief, pursuant to Section 1341(a) of the Internal Revenue Code (26 U.S.C. §1341(a) or IRC §1341(a)), in the aggregate amount of $78,688. This is a result of a $160,000 loss sustained while engaging in a trade or business resulting from the restitution payment to Blue Cross. The district court determined that because the restitution payment did not arise from the same facts, circumstances and conditions as Kraft's initial receipt of the money, they thereby are not entitled to IRC §1341 treatment. The district court did not address whether Kraft may be entitled to a deduction under another section of the Code. The United States Court of Appeals for the Sixth Circuit affirmed the findings.

II.

ARGUMENT

Supreme Court Rule 10 provides that: "A petition for writ of certiorari will be granted only when there are special portant reasons therefor." That rule further provides that typical nsiderations for granting certiorari include (1) when a United tes Court of Appeals has rendered a decision in conflict with the ision of another United States Court of Appeals on the same tter, or (2) when a United States Court of Appeals has so far arted from the accepted and usual course of judicial proceedings, sanctioned such a departure by a lower court, as to call for an rcise of this Court's power of supervision, or (3) when a United es Court of Appeals has decided an important question of federal which has not been, but should be, settled by this Court.

In the instant case, Appellants have sought the benefits ection 1341(a) of the Internal Revenue Code (IRC §1341(a)) to estitution payment made to Blue Cross. IRC §1341(a) provides if:

(1) an item was included in gross income for a prior taxable year (or years) because it appeared that the taxpayer had an unrestricted right to such an item;

(2) a deduction is allowed for the taxable year because it was established after the close of such prior taxable year (or years) that the taxpayer did not have an unrestricted to such item or to a portion of such item; and

(3) that the amount of such deduction exceeds $3,000,

then the tax imposed by this chapter for the taxable year shall be the lesser of the following:

(4) the tax for the taxable year computed with such deduction; or

(5) an amount equal to -

(A) the tax for the taxable year computed without such deduction, minus

(B) the decrease in tax under this chapter (or the corresponding provisions of prior revenues laws) or the prior taxable year (or years) which would result solely from the exclusion of such item

(or portion thereof) from gross income for such prior taxable year (or years).

IRC §1341 is the codification of the claim of right doctrine initially espoused in this Court's decision in *North American Oil Consolidated Co. v. Burnet*, 286 U.S. 417 (1932). The doctrine applies where a taxpayer receives money or other property without restriction on its disposition, although the taxpayer may have an imperfect right to retain such payment. If the taxpayer subsequently repays those amounts, the taxpayer may be entitled to beneficial tax treatment of the repayment pursuant to IRC §1341. The doctrine essentially provides the taxpayer with a refund in the year of repayment of taxes overpaid in earlier years. For example, assume an employee receives a commission of $30,000 in 1988. Subsequently, in 1990, it is determined that the employee's commission for 1988 should have been $26,000 and the employee is required to return the excess. Upon restoring the excess, the employee is entitled to recompute his tax liability for 1988 as if he had actually only received $26,000, and obtain a tax credit against 1990 taxes for the difference in tax liability.

In *North American Oil*, this Court stated that "if a axpayer receives earnings under a claim of right and without estriction to its disposition, he has received income which he is equired to [report on his] return, even though it may still be laimed that he is not entitled to retain the money and even though e may still be judged liable to restore its equivalent." *Id.* In *Healy . Commissioner*, 345 U.S. 278 (1953), this Court expanded its laim of right doctrine and provided that "there is a claim of right hen funds are received and treated by a taxpayer as belonging to im." This Court further explained that it would be inequitable to taxpayer to merely allow the taxpayer a deduction in the year of epayment as opposed to recomputing the tax liability for the year which the income was actually received and allowing a tax credit, ecause the taxpayer may be in a different tax bracket in the year of epayment and not receive the full benefit of the exclusion. These vo cases provided the foundation for the adoption of IRC §1341.

The district court granted summary judgment in favor the United States. The Sixth Circuit Court of Appeals affirmed. ne Court of Appeals based its decision on three grounds. First,

at pursuant to IRC §1341, a taxpayer must first demonstrate titlement to a tax deduction under another section of the Internal venue Code before invoking the claim of right doctrine. The urt found that Appellant failed to satisfy this requirement. The urt indicated that Appellants could not deduct the restitution yment under 26 U.S.C. §165(c)(1) (as claimed by Appellants) cause "losses arising from the repayment of fraudulently obtained ds are not deductible under 26 U.S.C. §165(c)(1)." In support, court cited various cases regarding return of embezzled funds. wever, there has never been any allegation that any funds were bezzled by Appellants, nor has there been any factual finding that amounts repaid by the Appellants were obtained through fraud. ther, the Court of Appeals, relying on its decision in *Bailey v. mmissioner*, 756 F.2d 44 (6th Cir. 1985), characterized the pellant's restitution payment as a payment of a penalty or fine and not deductible under 26 U.S.C. 162(a). This finding is contrary and in conflict with, the Second Circuit Court's holding in *hens v. Commissioner*, 905 F.2d 667 (2d Cir. 1990) as well as

the Tax Court's decision in *Joseph A. Barrett*, 96 T.C. No. 31 (1991).

Second, the Court of Appeals, based on its dictum in *Bailey*, erroneously concluded that the repayment of the funds did not arise out of the same circumstances, terms and conditions as the original receipt of the income.

Finally, the appeals court found that Appellants are not entitled to IRC §1341 treatment because Appellant did not have an unrestricted right to the funds because they were embezzled or otherwise knowingly misappropriated funds. Again, no such factual finding has been made.

The Court of Appeals' decision should be reviewed by this Court. The decision clearly conflicts with the decision of another circuit, thereby treating taxpayers differently on the basis of where they reside. The result of the lower courts rulings would deprive Appellant of its right to have factual questions decided by the trier of fact. The granting of summary judgment in the face of existing factual questions so far departs from the accepted and usual course of judicial procedure that this Court should review the matter.

The decision further effectuated the improper findings of the district court that all repaid funds were received fraudulently, to which there has not been a factual finding. The decision further upheld the erroneous conclusion of the district court that the restitution payment did not arise from the same circumstances, terms and conditions as Appellants' original receipt of the funds (though Appellants argue that this is not an actual requirement for treatment under IRC §1341). In essence, the decisions of the lower courts in this action have had the effect of using the tax laws to punish the taxpayers a second time, something this Court has expressly prohibited in *Commissioner v. Tellier*, 383 U.S. 687 (1966).

A. THE COURT OF APPEALS ERRED IN FINDING THAT APPELLANTS ARE NOT ENTITLED TO A DEDUCTION UNDER ANOTHER SECTION OF THE INTERNAL REVENUE CODE.

Under 26 U.S.C. §165(c)(1), losses incurred in the conduct of a trade or business are deductible. Appellants assert that all amounts paid by Kraft in restitution to Blue Cross are deductible thereunder. There has been no one definition of the term "trade or

usiness" that applies to all situations, and neither the law nor the egulations attempt one. However, in *Deputy v. DuPont*, 308 U.S. 88 (1940), this Court indicated that "trade or business" includes hose cases where the taxpayer holds himself out to others as ngaged in the sale of goods or services. As previously indicated, ll monies received from Blue Cross by Kraft were the result of ervices performed by Kraft and billed to Blue Cross. No allega- ons were ever set forth that Kraft did not in fact perform the ervices. The repayment resulted from a claim by Blue Cross that ervices were improperly billed, not that services were not per- ormed. In repaying Blue Cross, Appellants sustained a loss ncurred in the conduct of a trade or business in the amount of the epayment. The repayment was directly related to Kraft's actions as podiatrist. His trade or business was that of a podiatrist, and as uch, IRC §165(c)(1) allows a deduction in the amount of the epayment.

Appellant can additionally demonstrate entitlement to deduction of the restitution payment under 26 U.S.C. §162(a) as n ordinary and necessary expense paid or incurred in carrying on

trade or business. As discussed above, the restitution payment incurred in accordance with Kraft's trade or business of cticing podiatry. In addition, an amount paid in settlement of a m, arising from a business transaction, without admitting ility, for the purposes of avoiding litigation, is generally treated a business expense. *See* PH Federal Taxes 2nd ¶1624.040. rther, amounts paid in settlement of charges of civil fraud or proper conduct of a business, . . . are generally allowed as siness expenses. *Id*. *See* also *Helvering v. Hampton*, 79 F.2d 358 th Cir. 1935) (even if unethical conduct in business was extra-dinary, restitution therefor is ordinarily expected to be made from e person in the course of whose business the wrong was commit-d.) In *Helvering*, the court also distinguished between an amount aid in restitution for a wrong committed in the course of business, hich is an allowable deduction, and an amount paid as a fine or enalty, deduction of which is denied. *See* PH Federal Taxes 2nd]1624.040.

The Sixth Circuit Court mischaracterized the restitu-ion payment as that of a fine or penalty and thereby, pursuant to

RC §162(f), prohibited as a deduction. This is in clear conflict ith the Second Circuit's decision in *Stephens v. Commissioner*, 905 .2d 667 (2d Cir. 1990). In *Stephens*, the taxpayer sought to deduct epayment of embezzlement funds. The Commissioner maintained at public policy prevented such deduction. The court, in rejecting e Commissioner's position, held that "neither the public policy ception to Section 165, precluding a deduction when it would verely and immediately frustrate public policy to allow it, nor the odification of the public policy exception to deductibility of penses pursuant to Section 162, bars deduction of Stephens' stitution payment." *Id.* It further held that "Stephens' restitution yment is primarily a remedial measure to compensate another rty, not a 'fine or similar penalty,' even though Stephens repaid e embezzled funds as a condition of his probation" and the court stinguished *Bailey* stating "however, the payment in Bailey was iginally imposed as a fine and, in the view of the Sixth Circuit, ained its characteristic as a penalty despite its subsequent version to the class members." *Id.* The *Stephens* case makes it ar that public policy is not a bar to plaintiff's claims in their

omplaint, nor does Appellants' restitution payment rise to the level f the fine or penalty.

The restitution payment to Blue Cross is clearly not fin or a penalty. Kraft was actually assessed, and paid, additional mounts as penalties for which he has not sought a tax deduction. ather, this payment to Blue Cross was clearly restitutionary in fect and in no way can it be considered penal. It has been asserted at the restitution payment should be considered a penalty because e origin of liability was penal in nature. However, Kraft agreed make the restitution payment to Blue Cross prior to entering into e plea agreement and the plea agreement specifically refers to that ayment as a restitution payment, not a penalty. The payment was vil in nature and made to an independent organization. Pursuant IRC §162(f), only fines or similar penalties paid to the Govern- ent are not deductible, which is not applicable in the instant case.

The facts facing the lower courts fell squarely within e ambit of IRC §1341. Appellants had received, under a claim of ght, certain dollars, namely the $160,000 which Kraft later sgorged in restitution to Blue Cross. The amounts received by

Kraft were included in Appellants' tax returns as income for the elevant years and the appropriate taxes were paid on those amounts. At all times, Appellants believed, and it appeared that, they had an nrestricted right to the money. Subsequently, Kraft was required o restore the $160,000 of claimed (and previously taxed) income to lue Cross in the form of a restitution payment of amounts Blue ross claimed he did not have an unrestricted right to retain. This a prime example of the scenario which IRC §1341 is designed to ncompass.

Appellants' situation is remarkably similar to the facts f a recent Tax Court case, *Joseph A. Barrett*, 96 T.C. No. 31 991). In *Barrett*, the taxpayer was a securities broker who sgorged funds to settle a lawsuit brought against him as a result of leged insider trading. The taxpayer had, through a series of option ades over a two day period, netted profits in excess of $187,000 n a $2,000 investment) through alleged insider trading. Faced ith civil lawsuits and prosecution by the Securities Exchange ommission, the taxpayer paid $54,400 to settle the lawsuits and ve the S.E.C. terminate its administrative proceedings to remove

his brokerage license. The Tax Court found that pursuant to IRC §1341, the taxpayer was entitled to a credit in the settlement year equal to the decrease in tax for the earlier year (when funds were received and included in income) produced by removing those funds from income. The court found that the taxpayer had a subjective belief that he had an unrestricted right to the funds when he received them and that the taxpayer established that he did not have an unrestricted right to the funds in the year of repayment. The fact that he disgorged the funds as a result of settlement, rather than a judgment, did not affect this finding because a good faith non-collusive arms-length settlement had substantially the same effect as a judgment in the taxpayer's continued insistence that he did nothing wrong did not change that result. *Id.*

As further illustrated by the *Barrett* case, the test applied by the courts to determine applicability of IRC §1341 is (i) whether the taxpayer had a subjective belief that he had an unrestricted right to the funds when they were received and (ii) that the taxpayer establishes that he did not have an unrestricted right to the

funds in the year of repayment. It is a simple straightforward test.

The foregoing authorities explicitly support Appellants' claims in this matter. Similar to the taxpayers in *Barrett* and *Wetstone v. United States*, 5 AFTR 2d 1486 (1960), a comparable case, Appellant paid the restitution amount as a result of threatened and pending litigation, and pursuant to a "good faith" non-collusive arms-length settlement. No evidence was presented to establish that Kraft did not have a subjective belief that he had an unrestricted right to the funds when they were received, nor can it be argued that upon the payment of the restitution amount that Kraft did not in fact have an unrestricted right to the funds. Appellants are entitled to tax relief (as provided in IRC §1341) as a result of the repayment of the $160,000, which was originally earned by Appellant in pursuit of his trade or business as a podiatrist. This case is squarely "on all fours" with the facts in *Barrett*. That the lower courts did not follow that precedent and find in favor of the Appellants is inexplicable.

It is interesting to note that Appellee did not appeal the *Barrett* decision. Instead, when faced with the possibility of

osing this case on the same reasoning, Appellee issued a nonacqui-escence with the *Barrett* decision. The lower courts allowed hemselves to be diverted, ignored the mandate of *Barrett*, and nstead, relied on *Bailey*, a Sixth Circuit Court decision which, in ictum, set forth a factual test (whether the repayment arose from he same specific circumstances, terms and conditions as the ransaction whereby the funds were originally included in income) o determine whether a repayment of funds is entitled to IRC §1341 reatment. As a result, the lower courts made a factual determina-ion that Appellant did not satisfy the factual test set forth in *Bailey*, nd erroneously granted and affirmed Appellee's motion for ummary judgment. This was plain error. If, as the district court ecided, *Barrett* did not apply and *Bailey* did, the proper course vould have been to deny both summary judgment motions because actual questions were present, i.e. whether Kraft satisfied the actual test of *Bailey*, whether and to what extent there was fraud, tc. However, without any facts before it to justify such a finding, he lower courts found that the "dictum" test of *Bailey* was not met. This is improper.

Appellants assert that the facts before this court are irtually identical to those presented in *Barrett*, and therefore ppellant is entitled, as a matter of law, to the reversal of the order enying its motion for summary judgment and further reversing the rder granting Appellee's motion. With the expertise of the Tax ourt in interpreting the provisions of the Internal Revenue Code, eference should be given to that court's application of IRC §1341, articularly in such a closely related case.

This Court should address the split in the manner in hich this situation has been handled in different circuits (and the ax Court) and review this matter on its merits. It is unjust to xpayers in situations similar to Appellants to be penalized a second me merely because of domicile.

B. THE COURT OF APPEALS ERRED IN FINDING THAT APPELLANTS' REPAYMENT DID NOT ARISE OUT OF THE SAME CIRCUMSTANCES, TERMS AND CONDITIONS AS THE APPELLANTS' RECEIPT OF THE FUNDS.

The Court of Appeals further found Appellants not entitled to IRC §1341 treatment based upon dictum appearing in its decision in *Bailey*. The taxpayer in that case was denied IRC §1341 treatment because the taxpayer's return of income was declared a civil penalty by the court. Pursuant to IRC §1341, that section's benefits do not apply to repayment of penalties. Bailey had been involved in various deceptive and fraudulent trade practices and had entered into a consent decree with the Federal Trade Commission wherein he agreed to cease and desist from operating his business in deceptive and fraudulent manner. He subsequently violated that consent decree and was prosecuted. As a result, Bailey was fined $1,036,000, payment which was applied as restitution in settlement of various class action suits filed against the corporation and its officers for the fraudulent actions. In fact, the district court's order authorizing the use of the fine as restitution expressly stated that "the

ltimate disposition of these funds in no way shall alter their status
s civil penalties." *Id.* at 46. Bailey subsequently attempted to
aim that the payment of the $1,036,000 was entitled to IRC §1341
eatment. The Sixth Circuit held that Bailey was not entitled to IRC
1341 treatment because the payment arose from a judgment in a
it brought against the taxpayer by the Federal Trade Commission
recover civil penalties and that the taxpayer had therefore
rfeited the $1,036,000 amount as punishment for his violations of
e Federal Trade Commission Act. In essence, the payment was
erefore a fine imposed for purposes of enforcing the law, was a
nishment for violation of the law and, as such, was not deductible
nder the provisions of IRC §1341.

The instant matter is clearly distinguishable from
ailey. Appellant is not attempting to obtain IRC §1341 treatment
the payment of a penalty. Rather, as clearly indicated in the plea
greement, Appellants' payment to Blue Cross was a restitution
ayment. Kraft had previously paid a fine in this matter for which
has not sought a deduction (recognizing the relevant provisions).
ne payment to Blue Cross was a settled upon amount reached after

ms-length negotiations. It was civil in origin and compensatory in ture. No viable claim can be made that the payment was in any shion penal.

After making the determination that Bailey was not titled to IRC §1341 treatment of payment of his penalty, the court nt further and, in dictum, indicated that because the ultimate payment did not arise from the specific circumstances, terms and nditions of the transaction whereby the amount was originally luded in income, it did not qualify for IRC §1341 treatment. The urt found that Bailey's obligation to repay arose from the payer's violation of the consent decree, and not the original cumstances in which he included the compensation in his income. Appellee's urging, the district court in the instant matter grasped s concept and mistakenly found that Kraft was not entitled to IRC 341 treatment and the Court of Appeals affirmed. Appellant erts that this is not a requirement for treatment pursuant to IRC 341 as the language in question is not found in the text of the tion but rather solely in the Service's interpretive regulations. s Court should reverse the lower courts on those grounds.

However, even if the "circumstances, terms and conditions" test were an actual requirement pursuant to IRC §1341, Appellant's repayment to Blue Cross clearly arose from the specific circumstances, terms and conditions as Appellant's original receipt and inclusion of the income and therefore Appellant is entitled to IRC §1341 treatment. The lower courts' unsupported factual findings to the contrary are clearly departures from the usual course of judicial proceedings.

Appellee has argued that the payment to Blue Cross did not arise from the specific circumstances, terms and conditions as receipt of the income because the amount was originally included in income by Kraft as salary from the Corporation. Further, that the repayment was made pursuant to a plea agreement, not because the salary was received in error, and therefore the repayment did not arise from the specific circumstances, terms and conditions as the receipt of the income. Additionally, Appellee urges that Kraft never received any funds directly from Blue Cross, but rather the Corporation received the funds and included them in income. [It is worthy of note that the Corporation was also a defendant and that Blue

Cross insisted that payment come from Kraft.] However, a review of the appropriate facts and case law reveals the flaws in these assertions and findings.

First, funds were received directly by Dr. Kraft from Blue Cross. These funds were received as a result of surgical and non-surgical procedures performed on patients covered by Blue Cross. Kraft billed Blue Cross for these procedures and Blue Cross paid Kraft on those claims. Kraft took monies received directly from Blue Cross, funneled them through his professional corporation and subsequently withdrew his portion in the form of salary. As such, Kraft's initial receipt of the money was directly from Blue Cross and related to his claim for reimbursement for surgical and non-surgical procedures performed on Blue Cross participants. The important point here is that the funds paid by Blue Cross, the salary paid to Kraft by his corporation, AND the restitution paid by Kraft to Blue Cross ALL arose from the same specific circumstances, terms and conditions.

Blue Cross subsequently claimed that even though Kraft had performed the work (which fact has never been contested),

the monies paid to Kraft were paid under fraudulent conditions. To settle this claim, to avoid having to defend himself on two fronts, and to comply with the proposed plea arrangement, Kraft agreed to pay $160,000 in restitution to Blue Cross. This repayment arose directly from the same services for which Kraft was initially paid, those being the surgical and non-surgical procedures performed on patients who arguably were covered by Blue Cross. Had the taxpayer simply repaid his corporation and had the Corporation make the restitution payment to Blue Cross, the Government's reliance on the *Bailey* dictum would disappear (and both the taxpayer and the corporation would appear to have been entitled to their respective deductions). The Appellee should not be allowed to maintain this "form over substance" position. Appellant clearly satisfies any requirement that the repayment be from the specific circumstances, terms and conditions as the original receipt of income, and to find otherwise is clear error which must be re-dressed.

The issues addressed by the lower courts involved the resolution of factual questions. No basis existed to support any

findings relating to factual issues. Appellee did not file any affidavits with its summary judgment motion nor has any discovery taken place in this action. There simply has been no factual development of Appellee's case. To permit the summary judgment to stand in this instance would further a departure from the accepted and usual course of judicial proceedings to have factual disputes decided by the trier of fact after each side has had the opportunity to present its evidence. This Court should exercise its power of supervision to rectify this error.

C. THE COURT OF APPEALS ERRED IN FINDING THAT APPELLANTS DID NOT HAVE AN UNRESTRICTED RIGHT TO THE FUNDS WHEN THEY WERE RECEIVED.

The Court of Appeals found that Appellants are not entitled to IRC §1341 treatment because they did not have an unrestricted right to the money when it was received. The test for determining whether one has an unrestricted right to funds when they are received was clearly set forth in *McKinney v. United States*, 574 F.2d 1240 (5th Cir. 1978). That court established that the test

for determining an unrestricted right to an item of income is based upon the subjective belief of the taxpayer. In *McKinney*, the court ruled that "[t]he language of IRC §1341(a)(1), *i.e.*, 'because it appeared that the taxpayer had an unrestricted right to such item,' must necessarily mean 'because it appeared [to the taxpayer] that [he] had an unrestricted right to such item'." *Id.* Pursuant to the above test, the factual question to be resolved is whether when Kraft received the income initially from Blue Cross, it appeared to Kraft that he had an unrestricted right to the funds. The lower courts never made such factual determination. In fact, all actions taken by Kraft consistently supported his belief that he had an unrestricted right to the money.

The lower courts mistakenly equate this case to a long list of cases dealing with embezzlers. Under those cases, courts have found that IRC §1341 does not apply where a taxpayer has embezzled funds which he is later required to return because it could not have appeared to that taxpayer that he had an unrestricted right to money received through embezzlement. *See*, *McKinney*, *supra*. Unlike an embezzler, who knows from the outset that he has no

right to the funds, Kraft performed services which Blue Cross maintained were arguably inappropriate and/or improperly billed. However, the lower court is clearly wrong when it indicates that the appearance of an unrestricted right to an item depends on objective facts and circumstances, not on a taxpayer's subjective belief. This unquestionably is not in accord with the decision in *McKinney*. The *McKinney* test clearly states that it must appear to the taxpayer that he had an unrestricted right to such item. This explicitly indicates that what is required is solely the taxpayer's subjective belief that he had an unrestricted right to the item. This is a factual question to be decided by the trier of fact. The lower courts' ruling again creates a split in the Circuits.

In all the embezzlement cases cited by Appellee and relied on by the lower courts, the defendants had pled guilty or had been found guilty of embezzling the entire (or a substantial portion of the) amount which they sought to treat under IRC §1341. Thus, in those cases, it could not have appeared to those taxpayers that they had an unrestricted right to the funds. For example, in *Perez United States*, 51 AFTR 2d 83-519 (1982), the taxpayer was

ndicted on federal charges of mail fraud conspiracy. As a special ondition of his parole, Perez was required to make a restitution ayment of his ill-gotten gains. Perez sought IRC §1341 treatment f the amount restored. The court found that IRC §1341 did not pply because it could not have appeared to the taxpayer that he had n unrestricted right to the income because he knew they were ill-otten gains. In *Perez*, the plaintiff argued that trial was necessary n the issue of appearance of an unrestricted right. The court sagreed, finding that (unlike Kraft) there was no genuine dispute to the material fact of an appearance of an unrestricted right; no ich appearance could have existed (because Perez pled guilty as to e entire amount restored).

However, this situation is different. Although Kraft as charged with fraudulently obtaining $84,160, he pled guilty to aud ONLY in the amount of $1,358 (and Kraft claims only $19 of is amount was fraudulently obtained). Kraft repaid $160,000. No gument can logically be set forth that there is not a triable issue of ct as to whether Kraft had an unrestricted right to the money in cess of either $19 or $1,358. There has been no adjudication that

ne wrongfully obtained any such amounts and as such, there is bsolutely no basis to find that he could not have believed he had an nrestricted right to all or some portion of that money. As such, the ower courts erred in finding that Kraft did not have an unrestricted ight to the funds. At a minimum, this matter must be remanded for rial to determine what amount, if any, was fraudulently obtained by Kraft for which he could not have a belief that he had an nrestricted right to the money. In any event, the most that that mount could be is $84,160 (which is far less than $160,000). ermitting the summary judgment to stand in this instance would rther the departure from the accepted and usual course of judicial roceedings to have factual disputes decided by the trier of fact. his Court should exercise its power of review to rectify this error.

. THE COURT OF APPEALS ERRED IN AFFIRMING THE DISTRICT COURT'S GRANT OF SUMMARY JUDGMENT TO APPELLEE AS TO THE ENTIRE $160,000 RESTITUTION PAYMENT AS SIGNIFICANT FACTUAL QUESTIONS EXIST.

The indictment against Kraft charged him with audulently obtaining $84,160 through illegal billings to Blue Cross.

Of that amount, Kraft pled guilty to improperly billing $19 (for an x-ray), which amount was included in a check from Blue Cross totalling $1,358. As such, at the very least and assuming the very strongest position for Appellee (i.e., that the Appellee at trial could prove that the $84,160 was obtained through fraud), Appellant would be entitled to IRC §1341 treatment as to the remaining $75,840 of his repayment (and if such were the case, Appellant asserts that the $84,160 would properly be entitled to IRC §165(c)(1) treatment as a loss incurred in conducting a trade or business). Prior to issuing the indictment, the Government underwent an extensive investigation and charged Kraft with fraud only as to $84,160. Kraft, similar to the taxpayer in *Barrett*, paid in excess of what he believed he really owed as restitution to Blue Cross in an effort to settle pending litigation. It is clear that, in any case, any amounts above the $84,160 had to be received by Kraft under a belief that he had an unrestricted right to those monies. As to the remainder, on a dollar by dollar basis, the Appellee would have to prove two items to take any portion of the repayment out of the ambit of IRC §1341 - (i) that Kraft obtained the funds fraudulently, and (ii) that Kraft subjectively

elieved or knew that he obtained the funds improperly and did not ave an unrestricted right to the monies. Both items are questions f fact which should not have been decided on summary judgment sent any testimony or other documentary proof, which evidence as not before either court. Given the open factual questions, the ecisions of the lower courts depart from the accepted and usual ourse of judicial proceedings which require that such questions be solved by the trier of fact. Accordingly, this Court should exercise s power of supervision and review those decisions.

III.

CONCLUSION

This Court is respectfully requested to exercise its discretion and review this matter inasmuch as it involves an important question of federal law, namely the proper approach to implementation of 26 U.S.C. §1341 which has not been, but should be, settled by this Court. The Sixth Circuit Court's interpretation of that section is erroneous and has created a conflict between the Circuits. That court's treatment of Kraft's restitution payment as a penalty clearly conflicts with the Second Circuit (and the Tax) Court's treatment of similar payments. Further, the Sixth Circuit Court's application of its *Bailey* dictum circumvents the true intent of 26 U.S.C. §1341.

In essence, the decisions of the lower courts in this action have had the effect of using the tax laws to punish the Appellant a second time (by denying him the deduction to which he would otherwise be entitled pursuant to IRC §1341), something this Court has expressly prohibited in *Tellier*.

Additionally, this matter involves factual questions which have not been resolved. It has long been the rule that summary judgment is not proper when factual questions exist. Such questions are to be resolved by the trier of fact after each party has had the opportunity to present its evidence. However, both lower courts summarily concluded that all amounts repaid by Kraft were obtained fraudulently or else he would not have agreed to repay them. This overly simplistic approach is clearly in error as there has never been any factual determination as to what amount, if any, were obtained by fraud. Without such a determination, summary judgment cannot properly be granted. Circuit Judge Nelson, in his concurrence, recognized this fact as he stated "I have no problem with my colleagues' analysis if there is no genuine issue as to the fact -- asserted by the Government and denied by the taxpayers -- that Dr. Kraft defrauded Blue Cross of at least $160,000." Given the open factual questions, the decisions of the lower courts depart from the accepted and usual course of judicial proceedings so as to call for exercise of this Court's power of supervision.

As a result of the foregoing, to rectify the inequities suffered by the taxpayer, Appellants respectfully request this Court to grant their Petition for Writ of Certiorari to review this matter.

SHAPACK, MCCULLOUGH & KANTER, P.C.

By:_____

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Date: July 6, 1993

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APPENDIX

I. Order and Judgment of United States District Court for the Eastern District of Michigan

II. Opinion of United States Court of Appeals for the Sixth Circuit

III. Judgment of United States Court of Appeals for the Sixth Circuit

UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF MICHIGAN
SOUTHERN DIVISION

JESS AND BARBARA KRAFT,

Plaintiffs,

v. Civil No. 90CV73459DT

UNITED STATES OF AMERICA, Hon. Robert E. DeMascio

Defendant.
_____/

ORDER

ORDER

From approximately December 1973 through September 1985, plaintiff Jess Kraft, a licensed physician, practiced podiatry at the clinic of Joel H. Haber, D.P.M. and Jess Kraft, D.P.M., P.C., a Michigan Professional Corporation. Plaintiff's patients were covered by medical insurance through Blue Cross/Blue Shield of Michigan. Blue Cross payments for services rendered to patients were made to Haber and Kraft, individually, and the funds were then deposited to the corporation. The corporation billed Blue Cross $2,262,350.00 for the years 1981 through 1985.

In September 1984, a 34 count federal indictment was issued against Kraft, charging him with the illegal distribution of controlled substances and mail fraud. In 1985, an additional charge of mail fraud was filed against Kraft. On April 3, 1985, Kraft entered a plea agreement in which he pled guilty to one offense of distribution of a controlled substance under 21 U.S.C. § 841(a)(1) and one count of mail fraud under 18 U.S.C. § 1341. As part of the pleas bargain agreement, Kraft agreed to pay Blue Cross $160,000 as restitution.

On December 20, 1986, plaintiffs filed a claim for a tax refund in the amount of $78,000 contending that the $160,000 restitution payment was deductible under 26 U.S.C. § 1341 of the Internal Revenue Code. In June 1988, the plaintiffs filed an amended tax return for their 1985 tax return claiming a deduction of $37,550.77 for legal fees plaintiffs incurred in defending plaintiff Jess Kraft against criminal charges. Plaintiffs claim the legal fees were incurred as a result of Jess Kraft's trade or business and are deductible under 26 U.S.C. § 162(a). After the government's adverse ruling on both claims, the plaintiffs filed this suit seeking a refund of $78,688 computed after deducting the $160,000 restitution payment and a refund of $12,613.16 for the legal fees incurred in 1985. This matter is now before the court for consideration of cross motions of summary judgment.

26 U.S.C. § 1341 provides a special method for computing tax liability in circumstances where a taxpayer received an amount of income under a claim of right, included that sum as income, and in a subsequent taxable year was required to restore that amount because it was established that the taxpayer did not in fact have and unrestricted right to such amount. Bailey v. Commission-

er, 756 F.2d 44, 46 (6th Cir. 1985) (citing I.R.C. § 1341; Treas. Reg. § 1.1341.1)). For purposes of § 1341, income included under a claim of right means incomes included as part of gross income because it appeared from facts then available that the taxpayer had an unrestricted right to such income. Treas. Reg. 1.1341-1 (a)(2). The test for the application of §1341 is whether the obligation to repay arose from the same circumstances, terms and conditions of the transaction whereby the amount was included in income. Bailey v. Commissioner, 756 F.2d 44, 47 (6th Cir. 1985). It is clear that plaintiff Kraft's obligation to pay the $160,000 resulted from an obligation contained in a plea agreement.

Moreover, we find that 26 U.S.C. § 1341 does not support plaintiffs' claim to a deduction for the $160,000 because plaintiffs never made a claim of right to the money received from Blue Cross, a condition required under § 1341. Although Blue Cross made payments in Jess Kraft's name, he immediately deposited the funds directly to his professional corporation. The corporation reported the Blue Cross payments as taxable income. Plaintiff elected to receive his taxable income from the professional corporation which co-mingled the Blue Cross payments with funds

from other sources. Plaintiff never included the Blue Cross payments in his gross income. In other words, plaintiffs fail to meet the requirements for a deduction under § 1341 because plaintiffs' obligation to make restitution to Blue Cross did not arise out of the same circumstances, terms and conditions of his receipt of taxable income from the corporation.

However, plaintiffs' attorney fees incurred in the 1985 criminal action are deductible under 26 U.S.C. § 162(a). Attorney fees are deductible under § 162(a) if they relate to the conduct of the taxpayer's business activities. Commissioner v. Tellier, 383 U.S. 687, 689 (1966). Plaintiff was faced with a criminal indictment related to his business as a podiatrist. He had a constitutional right to defend himself by hiring legal counsel which resulted in the accumulation of attorney fees in the amount of $37,550.77. Such fees are deductible under 26 U.S.C. § 162(a).

Accordingly, the defendant's motion for summary judgment on the issue of whether plaintiffs are entitled to a deduction under 26 U.S.C. § 1341 is granted. Plaintiff's motion for summary judgment on the issue of whether they are entitled to a

deduction under 26 U.S.C. § 162(a) for attorney fees in the criminal action is granted and plaintiffs' complaint is dismissed.

IT IS SO ORDERED.

/s/
Robert E. DeMascio
United States District Judge

Dated: March 2, 1992

UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF MICHIGAN
SOUTHERN DIVISION

JESS AND BARBARA KRAFT,

Plaintiffs,

v. Civil No. 90CV73459DT

UNITED STATES OF AMERICA, Hon. Robert E. DeMascio

Defendant.
_____/

JUDGMENT

This matter came before the court on cross motions for summary judgment, and the court having filed its Order,

NOW, THEREFORE, IT IS ORDERED AND ADJUDGED

that defendant's motion for summary judgment on plaintiffs' claim to a deduction under 26 U.S.C. § 1341 be and the same hereby is GRANTED;

IT IS FURTHER ORDERED AND ADJUDGED

that plaintiffs' motion for summary judgment on plaintiffs' claim for a deduction under 26 U.S.C. § 162(a) be and the same hereby is GRANTED, and plaintiffs' complaint is hereby DISMISSED.

Dated at Detroit, Michigan, this 2nd day of March, 1992.

/s/
Robert E. DeMascio
United States District Judge

RECOMMENDED FOR FULL-TEXT PUBLICATION
Pursuant to Sixth Circuit Rule 24

No. 92-1552

UNITED STATES COURT OF APPEALS
FOR THE SIXTH CIRCUIT

JESS KRAFT and BARBARA KRAFT,
Plaintiffs-Appellants,

v.

UNITED STATES OF AMERICA,
Defendant-Appellee.

ON APPEAL from the United States District Court for the Eastern District of Michigan

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Decided and Filed April 7, 1993

Before: MERRITT, Chief Judge; NELSON, Circuit Judge; and CONTIE, Senior Circuit Judge.

CONTIE, Senior Circuit Judge, delivered the opinion of the court. MERRITT, Chief Judge (p. 17), and NELSON, Circuit Judge (p. 18), delivered separate concurring opinions.

CONTIE, Senior Circuit Judge. Jess and Barbara Kraft appeal the summary judgment dismissal of their 26 U.S.C. § 1341 claim for an income tax refund. For the following reasons, we affirm the district court's summary judgment dismissal.

I.

Plaintiff-appellant Jess Kraft ("Kraft"), a licensed physician, practiced podiatry at Joel H. Haber, D.P.M., and Jess Kraft, D.P.M., P.C., a Michigan professional corporation ("the Corporation"), from December, 1973 through September, 1985. Kraft, at all relevant times, was an employee, officer, director, and 50% shareholder of the Corporation. The Corporation was not a Subchapter S corporation.

From 1981 through 1984, the Corporation billed Blue Cross/Blue Shield of Michigan ("Blue Cross") approximately $2,245,000 for medical services performed by the Corporation. Once received, the Corporation included Blue Cross' payments in its gross income. The Corporation, in turn, paid Kraft wages for the fiscal years ending August 31, 1980 ($231,000), August 31, 1981 ($235,000), August 31, 1982 ($210,000), and August 31, 1983 ($249,000), which Kraft reported on the joint federal income tax returns he filed with his wife, plaintiff-appellant Barbara Kraft.

In September, 1984, a federal grand jury returned a 34-count Indictment charging Kraft with illegal distribution of controlled substances and mail fraud. Specifically, the Indictment alleged that Kraft performed unnecessary foot and toe surgeries on drug dealers and users by promising them Dilaudid, Percodan, and Demerol prescriptions. According to the Indictment, Kraft then submitted the bogus claims to Blue Cross which resulted in the wrongful payment of $84,160 to Kraft, though Blue Cross claims that Kraft actually defrauded it of $680,000, and Kraft claims that he "improperly billed" Blue Cross for only $19.

On or about April 3, 1985, the United States filed a one-count Information charging Kraft with mail fraud:

> That beginning in or about January of 1981, and continuing up to in or about November, 1983, Dr.

> Jess Kraft, D.P.M., defendant herein, devised and intended to devise a scheme and artifice to defraud Blue Cross/Blue Shield of Michigan and to obtain money through the use of false, fictitious and fraudulent pretenses and representations in the manner and means as follows:
>
> 1. At all times pertinent to this information, Jess Kraft, D.P.M., was a licensed podiatrist and operated two facilities doing business as Dr. Joel Haber, D.P.M., and Dr. Jess Kraft, D.P.M., P.C.
>
> 2. It was a further part of the scheme and artifice that Dr. Kraft, D.P.M., billed and caused to be billed Blue Cross/Blue Shield of Michigan for services purportedly rendered to persons insured by Blue Cross/Blue Shield of Michigan, when in truth, and as the defendant Dr. Jess Kraft, D.P.M., well knew, the services had been performed on different persons not insured by Blue Cross/Blue Shield of Michigan.
>
> That on or about August 13, 1983, in the Eastern District of Michigan, Southern Division, Jess Kraft, D.P.M., defendant herein, in furtherance of the aforesaid scheme and artifice to defraud and to obtain money by false and fraudulent representations, did cause to be placed in an authorized depository for mail, to be sent and delivered by the United States Postal Service, Blue Cross/Blue Shield of Michigan check number 008978836, in violation of Section 1341, Title 18, United States Code.

Information at 1-2.

On April 3, 1985, Kraft and the prosecutor executed a Rule 11 Plea Agreement ("Plea Agreement") whereby Kraft agreed to plead guilty to Count Eleven of the Indictment ("Distribution and Aiding and Abetting in the Distribution of Dilaudid") and Count One of the

Information ("Mail Fraud"). In return, the government agreed: to dismiss the remaining counts in the Indictment; to not seek forfeiture of Kraft's medical license; to limit Kraft's sentence to 15 years for Count Eleven of the Indictment, and 5 years for Count One of the Information, to run concurrently. The Plea Agreement also provided that "Dr. Kraft agrees to pay Blue Cross/Blue Shield of Michigan $160,000 restitution prior to sentencing pursuant to the Victim-Witness Protection Act of 1982." Rule 11 Plea Agreement at 2. On September 13, 1985, the district court sentenced Kraft to seven years imprisonment, and fined him $26,000.

On December 20, 1986, the Krafts filed Form 1040X ("Amended U.S. Individual Income Tax Return") with the Internal Revenue Service ("IRS") seeking a $78,688 tax refund for the 1985 tax year pursuant to Internal Revenue Code § 1341 (26 U.S.C. § 1341) which provides (in relevant part):

> § 1341. *Computation of tax where taxpayer restores substantial amount held under claim of right.*
>
> *(a) General rule.* --If--
>
> (1) an item was included in gross income for a prior taxable year (or years) because it appeared that the taxpayer had an unrestricted right to such item;
>
> (2) a deduction is allowable for the taxable year because it was established after the close of such prior taxable year (or years) that the taxpayer did not have an unrestricted right to such item or to a portion of such item; and
>
> (3) the amount of such deduction exceeds $3,000,

> then the tax imposed by this chapter for the taxable year shall be the lesser of the following:
>
> > (4) the tax for the taxable year computed with such deduction; or
> >
> > (5) an amount equal to --
> >
> > > (A) the tax for the taxable year computed without such deduction, minus
> > >
> > > (B) the decrease in tax under this chapter (or the corresponding provisions of prior revenue laws) for the prior taxable year (or years) which would result solely from the exclusion of such item (or portion thereof) from gross income for such prior taxable year (or years).

26 U.S.C. § 1341 (1988). The IRS denied the Krafts' claim:

> The claim of right has been disallowed since taxpayer knew at the time of filing the claim with Blue Cross and Blue Shield that he was not entitled to receive payment from the insurance company since wrong names were given to the company. Although the revenue ruling and court cases cited [above] deal mainly with embezzled funds, the facts clearly point that funds gained by wrongful or illegal means do not benefit from Section 1341 since the recipient knowingly accepted monies under false pretenses. Since the taxpayer submitted claims under false and fictitious individuals, he was aware that he had no "right" to the monies.
>
> Another factor in considering Dr. Kraft's case is the inclusion of the defrauded monies in income.

> The payments went to the corporation of the doctor's which he shared with another doctor. The funds were reported by the corporation and the taxpayer drew his salary from it. The possibility remains to exist that the corporation paid taxes on this money, the taxpayer received this money in his salary and the other doctor received this in his salary. There is no audit trail of these monies to determine who the recipient of the monies is.
>
> Section 165(c)(2) does allow a deduction as a non-business loss [the] restitution [of] illegally or wrongfully obtained monies, not a business loss. Only business losses qualify under Section 172 to be carried back as a net operating loss. Since the taxpayers' payment of the $160,000 would qualify as a non-business loss and not a business loss if allowed, the taxpayer is not entitled to claim a net operating loss back to 1981, 1982 and 1983 for the payback of funds to Blue Cross and Blue Shield.

Internal Revenue Service Form 886-A at 2-3.

The Krafts filed a second Form 1040X for 1985 seeking a $37,550.77 "ordinary and necessary trade or business expense" deduction, pursuant to 26 U.S.C. § 162(a), for legal fees paid defending against the criminal charges. The Internal Revenue Service denied this claim as well.

On November 27, 1990, the Krafts filed a Complaint against the United States in district court seeking a $91,301 income tax refund. Following cross-motions for summary judgment, the district court granted summary judgment to the United States with respect to Krafts' 26 U.S.C. § 1341 claim ($78,688), and granted summary judgment to the Krafts with respect to their 26 U.S.C. § 162(a) "ordinary and necessary trade or business expense" claim ($12,613):

> 26 U.S.C. § 1341 provides a special method for computing tax liability in circumstances where a

taxpayer received an amount of income under a claim of right, included that sum as income, and in a subsequent taxable year was required to restore that amount because it was established that the taxpayer did not in fact have an unrestricted right to such amount. For purposes of § 1341, income included under a claim of right means income included as part of gross income because it appeared from facts then available that the taxpayer had an unrestricted right to such income. The test for the application of § 1341 is whether the obligation to repay arose from the same circumstances, terms and conditions of the transaction whereby the amount was included in income. It is clear that plaintiff Kraft's obligation to pay the $160,000 resulted from an obligation contained in a plea agreement.

Moreover, we find that 26 U.S.C. § 1341 does not support plaintiffs' claim to a deduction for the $160,000 because plaintiffs never made a claim of right to the money received from Blue Cross, a condition required under § 1341. Although Blue Cross made payments in Jess Kraft's name, he immediately deposited the funds directly to his professional corporation. The corporation reported the Blue Cross payments as taxable income. Plaintiff elected to receive his taxable income from the professional corporation which co-mingled the Blue Cross payments with funds from other sources. Plaintiff never included the Blue Cross payments in his gross income. In other words, plaintiffs fail to meet the requirements for a deduction under § 1341 because plaintiffs' obligation to make restitution to Blue Cross did not arise out of the same circumstances, terms and conditions of his receipt of taxable income from the corporation.

However, plaintiffs' attorney fees incurred in the 1985 criminal action are deductible under 26

> U.S.C. § 162(a). Attorney fees are deductible under § 162(a) if they relate to the conduct of the taxpayer's business and the criminal charges are based upon the taxpayer's business activities. Plaintiff was faced with a criminal indictment related to his business as a podiatrist. He had a constitutional right to defend himself by hiring legal counsel which resulted in the accumulation of attorney fees in the amount of $37,550.77. Such fees are deductible under 26 U.S.C. § 162(a).

District Court's March 2, 1992 Order at 3-4 (citations omitted).

The Krafts timely filed a notice of appeal challenging the district court's 26 U.S.C. § 1341 "claim of right" determination. The United States has not appealed the district court's 26 U.S.C. § 162(a) determination.

II.

Summary Judgment

Summary judgment is appropriate where "there is no genuine issue as to any material fact and . . . the moving party is entitled to judgment as a matter of law." Fed. R. Civ. P. 56. A district court's grant of summary judgment is reviewed *de novo*. *Pinney Dock & Transp. Co. v. Penn Cent. Corp.*, 838 F.2d 1445, 1472 (6th Cir.), *cert. denied*, 488 U.S. 880 (1988). In its review, this court must view all facts and inferences drawn therefrom in the light most favorable to the nonmoving party. *60 Ivy St. Corp. v. Alexander*, 822 F.2d 1432, 1435 (6th Cir. 1987).

The moving party has the burden of conclusively showing that no genuine issue of material fact exists. *Id.* Nevertheless, in the face of a summary judgment motion, the nonmoving party cannot rest on its pleadings but must come forward with some probative evidence to support its

claim. *Celotex Corp. v. Catrett*, 477 U.S. 317, 324 (1986); *60 Ivy St. Corp.*, 822 F.2d at 1435.

"By its very terms, this standard provides that the mere existence of *some* alleged factual dispute between the parties will not defeat an otherwise properly supported motion for summary judgment; the requirement is that there be no *genuine* issue of *material* fact." *Anderson v. Liberty Lobby, Inc.*, 477 U.S. 242, 247-48 (1986) (emphasis in original). The dispute must be genuine and the facts must be such that if they were proven at trial, a reasonable jury could return a verdict for the nonmoving party. *60 Ivy St. Corp.*, 822 F.2d at 1435. If the disputed evidence "is merely colorable or is not significantly probative, summary judgment may be granted." *Anderson*, 477 U.S. at 249-50 (citations omitted).

Dr. Kraft's Claim Under 26 U.S.C. § 1341

On appeal, the appellants maintain that they are entitled to recompute their 1985 tax liability pursuant to 26 U.S.C. § 1341:

> The facts facing the district court on appellants' motion for summary judgment fell squarely within the ambit [of] Section 1341. Appellants had received, under a claim of right, certain dollars, namely the $160,000 which Kraft later disgorged in restitution to Blue Cross. The amounts received by Kraft were included in appellants' tax returns as income for the relevant years and the appropriate taxes were paid on those amounts. At all times, appellants believed, and it appeared that, they had an unrestricted right to the money. Subsequently, Kraft was required to restore the $160,000 of claimed (and previously taxed) income to Blue Cross in the form of a restitution payment of amounts Blue Cross claimed he did not have an unrestricted right to retain. This is a prime

example of the scenario which Internal Revenue Code section 1341 is designed to encompass.

. . . .

[T]he test applied to determine the applicability of Section 1341 is (i) whether the taxpayer had a subjective belief that he had an unrestricted right to the funds when they were received, and (ii) that the taxpayer establishes that he did not have an unrestricted right to the funds in the year of repayment. It is a simple straightforward test.

. . . .

[T]he payment to Blue Cross clearly arose from the same circumstances, terms and conditions as the original receipt and inclusion of the income. Kraft initially received the monies from Blue Cross as a result of surgical and non-surgical procedures performed on patients covered by Blue Cross. Kraft billed Blue Cross for these procedures. Blue Cross paid Kraft on these claims, which money was then funnelled through Kraft's professional corporation and then repaid to Kraft in the form of salary. Blue Cross subsequently claimed that the monies paid to Kraft were paid under fraudulent conditions. As a result, [Dr. Kraft] agreed to repay $160,000 to Blue Cross. The repayment arose directly from the same services for which Kraft was initially paid. As such, Kraft clearly satisfies this aspect of the IRC § 1341 test.

Judge DeMascio erroneously found that because the funds were deposited by Kraft directly into the corporation where they were allegedly commingled with other funds of the corporation . . . prior to disbursing to Kraft in the form of salary, that Kraft did not have a claim of right to those funds. Judge DeMascio then asserts that the corporation reported the money as income, not Kraft.

> However, this overlooks the true substance of the transaction and accepts the appellee's "form over substance" argument. In reality, when Kraft reported the salary received from his professional corporation as income, and filed tax returns, he was, in actuality, reporting the money received from Blue Cross.

Appellants' Brief at 8-15 (citations omitted).

In response, the United States argues: that Dr. Kraft's restitution payment did not arise from the same circumstances, terms and conditions as Kraft's original receipt of income; that Kraft may not disregard the tax disadvantages of the corporate entity; that funds obtained by fraud are not obtained under a "claim of right"; and, that Kraft may not deduct the $160,000 payment under any other provision of the Internal Revenue Code (a prerequisite to applying 26 U.S.C. § 1341).

Specifically, the United States maintains:

> The restitution payment did not arise from the same circumstances, terms, and conditions as Kraft's original receipt of income. The item originally included in income was Kraft's salary from the Corporation. There has been no contention that Kraft's salary was paid in error, and Kraft has never had any obligation to return any portion of it for the years in issue. Nor has he done so. The $160,000 payment was not a return of "items" included on taxpayers' return and was not computed with reference to Kraft's salary, but was a payment to Blue Cross made as part of a plea agreement "in settlement and restitution of any and all civil claims of Blue Cross against Kraft and the Corporation." Kraft never received any funds directly from Blue Cross. It was the Corporation which did so and included these payments in its income. Thus, it is clear that taxpayers do not qualify for § 1341 treatment.

Taxpayers contend that although the Blue Cross funds, in form, were paid to the Corporation, in substance, they were received by Kraft, albeit in the form of salary payments, and that this Court should ignore the form and look at the substance. But it is settled that when a taxpayer has chosen to incorporate to do business, he must accept the tax disadvantages and cannot disregard the corporate entity even where there is only one shareholder.

. . . .

Section 1341 is inapplicable even if the corporate entity can be disregarded because funds obtained by fraud are not obtained under a claim of right. Section 1341, by its terms, applies only where it "appeared that the taxpayer had an unrestricted right to such item" of income. The courts have repeatedly held that § 1341 has no application where a taxpayer has embezzled or otherwise knowingly misappropriated funds which he is later required to return because it could not have "appeared" that the taxpayer had an unrestricted right to the money so obtained. . . . The appearance of an unrestricted right to an item depends on objective facts and circumstances, not on a taxpayer's subjective belief.

It is undisputed that some, if not all, of the $160,000 payment was initially obtained by fraud. . . . Section 1341 is inapplicable to the extent that Kraft obtained money fraudulently from Blue Cross since it could not have appeared to him that he had an unrestricted right to the money so obtained.

. . . .

It is settled that for § 1341 to apply, the taxpayer must be entitled under some other provision of the Internal Revenue Code to a deduction for the

> payment in that year. [T]he courts have uniformly held that losses arising from repayment occasioned by fraudulent activity are not deductible under § 165(c)(1). . . . [F]raudulently obtaining funds from Blue Cross is no more the proper function of the trade or business of being a podiatrist than is embezzlement the proper function of the trade or business of being a salaried employee or a legitimate securities trader. Thus, the restitution payments are not deductible under § 165(c)(1).

Appellee's Brief at 15-23 (citations omitted).

In *Bailey v. Commissioner*, 756 F.2d 44 (6th Cir. 1985), this court denied 26 U.S.C. § 1341 tax relief to a taxpayer ordered to pay a $1,036,000 fine (later deemed a restitution to settle a civil action) for violating the terms of a consent decree. Though the Krafts attempt to distinguish *Bailey*, we see no reason to depart from its holding.

"Before invoking § 1341, the taxpayer must be entitled under some provision of the Internal Revenue Code to a deduction for the restoration payment in that year." *Bailey v. Commissioner*, 756 F.2d at 46 (citations omitted). Though the Krafts argue that "all amounts paid by Dr. Kraft in restitution to Blue Cross are deductible," Appellants' Reply Brief at 17-18, under 26 U.S.C. § 165(c)(1) ("losses incurred in a trade or business") because "[t]he repayment was directly related to Kraft's actions as a podiatrist," Appellants' Reply Brief at 18, losses arising from the repayment of fraudulently obtained funds are not deductible under 26 U.S.C. § 165(c)(1). *See Mannette v. Commissioner*, 69 T.C. 990 (1978) (the repayment of embezzled funds is not deductible under section 165(c)(1) as a "trade or business" loss). Though the repayment of embezzled funds may be deductible under section 165(c)(2) ("losses incurred in any transaction entered into for profit, though not connected with a trade or business"), the deductibility of nonbusiness losses under section 165(c)(2) is limited to the amount of

gross income not derived from the trade or business. Because the Krafts reported no nonbusiness income in 1985, 26 U.S.C. § 165(c)(2) offers them no benefit.

Though the Krafts maintain that they can demonstrate an "entitlement to a deduction of the restitution payment under 26 U.S.C. § 162(a) as an ordinary and necessary expense paid or incurred in carrying on any trade or business," Appellants' Reply Brief at 18, their ability to do so hinges on the applicability of 26 U.S.C. § 162(f) ("Fines and penalties") which provides that "[n]o deduction shall be allowed under subsection (a) for any fine or similar penalty paid to a government for the violation of any law." *Compare Stephens v. Commissioner*, 905 F.2d 667, 671 (2d Cir. 1990) ("taxpayers who repay embezzled funds are ordinarily entitled to a deduction in the year in which the funds are repaid" if the restitution is primarily a remedial measure to compensate another party, not "a fine or similar penalty") *with Bailey v. Commissioner*, 756 F.2d at 47 ("the characterization of a payment for purposes of § 162(f) turns on the origin of the liability giving rise to it").

Dr. Kraft agreed "to pay Blue Cross/Blue Shield of Michigan $160,000 restitution prior to sentencing pursuant to the Victim-Witness Protection Act of 1982." Rule 11 Plea Agreement at 2. Though the Krafts maintain that this payment does not constitute a penalty, Sixth Circuit precedent establishes that Dr. Kraft's restitution payment arose out of criminal proceedings thereby constituting a non-deductible penalty. *See Bailey v. Commissioner*, 756 F.2d at 47 ("Bailey, therefore, forfeited the $1,036,000 as punishment for his violations of the Federal Trade Commission Act, and the payment was thus a fine imposed for purposes of enforcing the law and as punishment for a violation thereof.").

Moreover, the Krafts are precluded from invoking 26 U.S.C. § 1341 because Dr. Kraft paid $160,000 to Blue Cross as part of his Plea Agreement (relating to mail

fraud and drug trafficking charges) which did not result from the same "circumstances, terms and conditions" as his salary from the Corporation.

It is unclear whether Blue Cross remitted its payments directly to the Corporation or to Dr. Kraft individually. *Compare* Appellants' Brief at 2 ("Payment for services rendered to Blue Cross was generally made by Blue Cross directly to doctors Haber and Kraft, individually, and they then deposited those monies into the Corporation.") *with* Appellee's Brief at 16 ("Kraft never received any funds directly from Blue Cross. It was the Corporation which did so and included these payments in its income.") *and* Indictment at 28-29 (Blue Cross remitted its payments to "Kraft PC Jess DPM"). We need not resolve this conflict, however, because the Blue Cross payments were deposited, at some point in time, in the Corporation's bank accounts where they were commingled with other funds and used to pay the Corporation's expenses, including the doctors' salaries. Dr. Kraft did not report the Blue Cross payments on his individual income tax returns; he reported his salary from the Corporation.

The Sixth Circuit previously summarized this rationale:

> Taxpayer is precluded from invoking § 1341 for another reason. [T]he taxpayer's obligation to repay must arise out of the specific "circumstances, terms and conditions" of the transaction whereby the amount was originally included in his income. The $1,036,000 Bailey paid in 1977 was a civil penalty imposed under 15 U.S.C. § 45 for his multiple violations of an FTC consent order. The payment, therefore, arose from the fact that Bailey violated the consent order, and not from the "circumstances, terms and conditions" of his original receipt of salary and dividend payments from Bestline. Indeed, the amount of the penalty was not computed with reference to the amount of his salary, dividends,

> and bonuses, and bears no relationship to those amounts.

Bailey v. Commissioner, 756 F.2d at 47 (citations omitted). Indeed, we may fairly infer from this language this court's unwillingness to abandon the separate identities of a corporation and its owner-employee.

Furthermore, 26 U.S.C. § 1341 does not apply to a taxpayer who has embezzled or otherwise knowingly misappropriated funds which he is later required to return because the taxpayer never had an unrestricted right to the money so obtained. *See McKinney v. United States*, 574 F.2d 1240, 1243 (5th Cir. 1978) ("When the item was embezzled funds, it is clear that it could not appear *to the taxpayer* that he had *any* right to the funds, much less an unrestricted right to them. This contention is consistent with the applicable regulations.") (emphasis in original), *cert. denied*, 439 U.S. 1072 (1979).

Jess and Barbara Kraft failed to set forth a genuine issue of material fact relevant to their 26 U.S.C. § 1341 claim. Accordingly, the district court properly granted the United States' motion for summary judgment.

III.

We AFFIRM the district court's summary judgment dismissal of the Krafts' 26 U.S.C. § 1341 claim for the aforementioned reasons.

MERRITT, Chief Judge, concurring. I concur basically in the reasons stated in Judge Contie's opinion for denying the Krafts' petition for a refund. I find the most clearly reasoned and persuasive case on this subject to be *Perez v. United States*, 553 F. Supp. 558 (M.D. Fla. 1982). There the president of a corporation who pled guilty to mail fraud and as a condition of parole was required to make restitution for kickbacks was not allowed a lost deduction for the amounts paid in satisfaction of the restitution requirement. That case appears to be directly in point. In a clear opinion by Judge Krentzman, the court reviewed the legislative history and development of § 1341. It shows that Congress enacted this section in order to overrule the case of *Lewis v. Commissioner*, 340 U.S. 590 (1951). It also shows that in enacting § 1341 Congress did not intend to overrule the "claim of right" doctrine. The court concluded "that Congress could not have intended to extend 1341 to embezzlers, for their income was not even taxable in 1954." 553 F. Supp. at 561. Thus for the reasons stated in Judge Contie's opinion and for the reasons stated in the *Perez* opinion, I would affirm the judgment of the District Court.

DAVID A. NELSON, Circuit Judge, concurring. I have no problem with my colleagues' analysis if there is no genuine issue as to the fact -- asserted by the government and denied by the taxpayers -- that Dr. Kraft defrauded Blue Cross of at least $160,000. I consider it unnecessary to decide whether there is any genuine issue as to the amount of the fraud, however, because I do not believe that the Krafts come within the terms of 26 U.S.C. § 1341 in any event.

For a taxpayer to take advantage of § 1341, he must show, among other things, (1) that "an item" was included in a prior year's gross income because of an apparent unrestricted right to the item, and (2) that it was subsequently established that the taxpayer did not have an unrestricted right to "such item" or a portion thereof. 26 U.S.C. §§ 1341(a)(1) and (a)(2). Both sections clearly speak of the same "item."

The "item" included in the Krafts' gross income for the prior year at issue here was not a fee received from Blue Cross; it was, rather, a salary item received by Dr. Kraft from his corporation. It has not been established that Dr. Kraft had no unrestricted right to his salary as far as the corporation is concerned, and there is no contention that Dr. Kraft ever remitted any part of his salary to the corporation. It was Dr. Kraft's decision to use his corporation as a source of income, and on the facts of this case I can see no justification for piercing the corporate veil and pretending that there was never any corporation in the picture. I would affirm the judgment of the district court on that basis.

UNITED STATES COURT OF APPEALS
FOR THE SIXTH CIRCUIT

No: 92-1552

JESS KRAFT and BARBARA KRAFT,

Plaintiffs - Appellants,

v.

UNITED STATES OF AMERICA,

Defendant - Appellee.

Before: **Merritt,** Chief Judge; **Nelson,** Circuit Judge;
Contie, Senior Circuit Judge

JUDGMENT

ON APPEAL from the United States District Court for the Eastern District of Michigan at Detroit.

THIS CAUSE was heard on the record from the district court and was argued by counsel.

ON CONSIDERATION WHEREOF, it is ordered that the judgment of the district court is affirmed.

ENTERED BY ORDER OF THE COURT

/s/
Leonard Green, Clerk

Issued as Mandate: **5-03-93**

COSTS: None

Filing Fee.....$
Printing.....$

TOTAL.....$